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WAITING FOR THE CROP PRODUCTION REPORT

On August 11, the USDA will release the first corn and soybean yield and production forecasts for the 2006 crops that are based on survey and field observation data. Private forecasts generally reflect expectations that the report will show potential for average yields to be slightly above trend for both crops.

At the end of July, the USDA's weekly report of crop conditions showed that 56 percent of the U.S. corn crop was in good or excellent condition. That compares to 53 percent at the same time last year and 57 percent at the end of the season last year. Based on the best fit between the percentage of the crop rated good or excellent at the end of the season and the U.S. average yield since 1986, a rating of 56 percent at the end of the 2006 season would suggest a yield near 145 bushels, about 4 bushels below trend. However, the U.S. average yield has exceeded the yield forecast by crop condition ratings for 7 consecutive years. The difference has ranged from 0.4 bushels to 7.4 bushels, averaging 3.3 bushels. That pattern might point to a yield near 148 bushels if condition ratings at the end of the season are near those at the end of July. Each percentage point change in the portion of the crop rated good or excellent would alter the yield expectation about .65 bushels.

At the close of trade on August 4, the corn futures market reflected a 2006-07 marketing year average farm price near $2.65. That calculation assumes that the relationship between the monthly average price received by producers and the average monthly price of the nearby futures contract is at the average of the past 5 years. In addition, it assumes that producers market the 2006 crop in a monthly pattern similar to the average of the past five years. Based on the relationship between the year ending stocks-to-use ratio and the marketing year average price since 1998-99, a price of $2.65 implies a stocks-to-use ratio of 7.8 percent at the end of the 2006-07 marketing year. If use is near the 11.735 billion bushels projected by USDA, the current price reflects a September 1, 2007 inventory of only 915 million bushels, implying an average yield of 146.7 bushels. The market appears to be trading an average yield below trend value or is anticipating stronger demand than reflected by the USDA projections.

At the end of July, the USDA's weekly report of crop conditions showed 53 percent of the soybean crop in good or excellent condition. That compares to 54 percent at the same time last year and 57 percent at the end of the 2005 growing season. A rating of 53 percent good or excellent at the end of the 2006 season would suggest a yield near 41 bushels, slightly higher than the USDA's calculated trend value of 40.7 bushels. Each percentage point change in the portion of the crop rated good or excellent would alter the yield expectation about 0.2 bushels.

At the close of trade on August 4, the soybean futures market reflected a 2006-07 marketing year average price near $5.95, under the same assumptions as outlined for corn. The relationship between the year-ending stocks-to-use ratio and marketing year average farm price has not been as stable for soybeans as for corn. The average price during the current year, for example, will be about $.25 higher than projected by the stocks-to-use ratio. The instability in that relationship makes it more difficult to calculate the yield currently being traded by the market. The USDA projects a 2006-07 year ending stocks-to-use ratio of 18.7 percent. Based on historic relationships, that ratio points to a 2006-07 marketing year average farm price near $5.40. The current soybean futures prices for the 2006-07 marketing year appear to reflect some combination of below trend yield, continued strong speculative demand, or larger consumption of U.S. soybeans during the year ahead.

Pointing to the generally weak new crop corn basis and the potential to significantly reduce inventories during the year ahead, most analysts are suggesting that producers plan to store a large portion of the new crop in anticipation of higher cash prices. With a large carry in the market and the resulting sharply higher prices for delivery in 2007, however, the question is whether the stored crop should be unpriced or forward priced for later delivery to capture the higher prices already offered.

The soybean situation is more complicated. Unless the U.S. average yield falls well below trend, surpluses will continue, assuming a normal South American growing season. Potential for much higher prices may be less than for corn. In addition, the premiums for post-harvest delivery are not as large as for corn, even though the new crop basis is generally weak. Under current price relationships, physical storage of soybeans beyond harvest is not as attractive as storage of corn. Ownership beyond harvest with futures or basis contracts may be less expensive than storage if the carry remains small.

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